No. 10272

In the United States Circuit Court of Appeals for the Ninth Circuit

SAN FERNANDO MISSION LAND COMPANY, A CORPORATION,
PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

ON PETITION FOR REVIEW OF THE DECISION OF THE UNITED STATES BOARD OF TAX APPEALS

BRIEF FOR THE RESPONDENT

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CITATIONS

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OPINION BELOW

The only previous opinion in this case is the memorandum opinion of the United States Board of Tax Appeals (R. 14–19), which is not reported.

JURISDICTION

The petition for review herein involves a deficiency in excess profits tax liability in the sum of $8,035.64 [1]

[1] The case before the Board of Tax appeals involved deficiencies in both income and excess profits tax liabilities in the respective amounts of $4,508.56 and $8,035.64 for the taxable year 1938. (R. 14.) Two other issues (involving commissions and attorney's fees paid by the taxpayer) were decided adversely to the taxpayer by the Board (R. 19) and are now conceded and have been abandoned by the taxpayer (Br. 2). There remains therefore the single issue presented herein, stated hereinafter, involving a deficiency

asserted against the taxpayer for the taxable year 1938 by the Commissioner of Internal Revenue in notice of deficiency mailed February 8, 1941. (R. 8–12, 14.) Within ninety days thereafter and on May 5, 1941, the taxpayer filed a petition with the Board of Tax Appeals for a redetermination of that deficiency under the provisions of Section 272 of the Internal Revenue Code. (R. 4–12.) The final order and decision of the Board of Tax Appeals sustaining the deficiency, was entered on May 25, 1942 (R. 20), the taxpayer's motion for revision and review filed June 18, 1942 (R. 21–31) having been denied by the Board on June 19, 1942 (R. 32). The case is brought to this Court by petition for review filed July 24, 1942 (R. 33–42), pursuant to the provisions of Sections 1141 and 1142 of the Internal Revenue Code.

QUESTION PRESENTED

Whether the taxpayer was "carying on or doing business" during any part of the capital stock tax year ended June 30, 1938, within the meaning of Section 601 (a) of the Revenue Act of 1938, so that it is subject to an excess profits tax liability for the calendar year 1938 imposed by Section 602 (a) of that Act.

STATUTE AND REGULATIONS INVOLVED

The statute and regulations involved are set forth in the Appendix, *infra,* pp. 23–27.

STATEMENT

The facts as found by the Board of Tax Appeals (R. 14–17) are as follows:

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in excess profits tax in the sum of $8,035.64 for the taxable year 1938. (Br. 2.)

Taxpayer is a California corporation with principal office at Los Angeles, California, and filed its 1938 income tax return with the Collector there. It was organized in 1904 to buy, develop, and sell land; it acquired over 16,000 acres about fifteen miles from the center of Los Angeles, and engaged actively and successfully in the development and sale of this tract. In 1918 it declared a dividend of $1,000,000 which it paid by a distribution of lands among its shareholders. Thereafter it donated some land to the city for parks, restricted its business activity, reduced its capitalization from $1,000,000 to $100,000, and distributed $1,250,000 in a series of dividends, the last being one of $100,000 paid on January 29, 1923. Few assets remained, and shareholders displayed little interest in the corporation, but it was not dissolved. After a meeting on February 2, 1927, the directors did not again meet for nearly a decade. On state franchise tax returns, taxpayer was described as "practically liquidated."

Taxpayer's remaining properties after 1930 consisted of a thirty-five acre grove of orange and lemon trees, 138 acres of unplotted hill lands, reservations of mineral rights in some 3,000 acres of land previously sold, and a very small amount of cash. The grove was in poor condition, unprofitably operated for many years, and in 1937 the trees were uprooted and it was abandoned to the state for unpaid taxes. The hill lands lying some twenty miles from the center of Los Angeles were without improvements or available water. Of the original acreage, they constituted a part for which no buyer was found. The grove and these lands were carried on taxpayer's books at $52,500 and $13,800, respectively. The

reservations of mineral rights were carried at one dollar. In selling its real estate, taxpayer had in some cases reserved mineral rights and as in early years had authorized its officers to execute oil and gas leases. The board of directors in 1925 gave consideration to proposals for oil leases, and at the meeting on February 2, 1927, they considered several proposals and ratified a release of the reserved rights in certain land for a consideration of $2,940. At the same time they resolved to make no more such releases "for the present, at least."

After 1930, taxpayer operated the grove at a continual loss; in 1932 it made one sale of realty for about $1,500; in 1935 it rented pasture for $75, and in 1936 it received $7,500 for release of oil reservations and for a lot. Taxes and expenses exceeded income except in 1936, and the balance sheet constantly showed a deficit of about $40,000 during the period. In 1936 no oil had been found on or near taxpayer's properties and no survey for oil had been made. At the instigation of the president of one of taxpayer's creditors, the directors met on September 14, 1936, and elected him president. He entered into negotiations for the leasing of oil rights. A lease, authorized by the directors and placed in escrow on November 10, 1937, was not delivered because of the lessee's failure to perform conditions. On his initiative, the grove was abandoned in the fall of 1937.

During the fiscal year July 1, 1937–June 30, 1938, taxpayer received $51.87 in the sale of fruit; $50 from the rental of pasture; and two other small items. From

the sale of 4.75 acres of the hill lands it realized a profit of $1,890 and in the sale of reserved oil rights it received $1,180. Its total income was $3,270.66, and its expenses and taxes were $2,897.34. On March 16, 1938, taxpayer made a twenty-year lease of oil rights for royalties which are being paid. On August 26, 1938, it made a lease of oil rights for $20,000 and royalties from oil as long as produced.

Taxpayer received income from its leases in 1938, 1939 and 1940, and declared dividends in each of those years.

In the fiscal year ending June 30, 1938, taxpayer was carrying on and doing business.

On August 26, 1938, taxpayer employed Robert V. New to promote and negotiate oil leases. His compensation was to be based on the amount of rental. Through New's efforts, taxpayer made a lease of oil rights on November 25, 1938, for a minimum period of twenty years, receiving $76,130 and the right to a royalty. Pursuant to the employment agreement, taxpayer paid New $33,306.88 for negotiating this lease and paid an attorney $250 for preparing the instrument.

Upon the basis of the foregoing facts the Board held that the taxpayer corporation carried on or did business during the year ended June 30, 1938, and therefore it was properly subjected to the excess profits tax liability in question for the calendar year 1938. (R. 19.) The Board thereupon entered its decision accordingly (R. 20) from which the taxpayer petitioned this Court for review (R. 33).

SUMMARY OF ARGUMENT

Under the pertinent regulations, the taxpayer's activities during the fiscal year ended June 30, 1938, constituted carrying on and doing business within the meaning of the statute The regulations, consistently applied administratively since 1918, have been held to be a reasonable and permissible construction of the act. The Board found as a fact and concluded that the taxpayer was carrying on and doing business during the critical period. Its findings are supported by substantial evidence. They should therefore be affirmed.

Selling, renting and managing real estate and making leases for cash and collecting royalties therefrom have been held to be doing business within the meaning of the statute. The taxpayer not only merely owned property and engaged in conduct incidental to the distribution of the avails but engaged in many other activities of a profitable business nature.

The fact that the taxpayer might have *intended* to liquidate its properties some time or other, does not mean that it was not engaged in business. Since it was engaged in activities ordinarily carried on for profit, it is immaterial whether it was making a profit or intended eventually to liquidate. In fact, however, the taxpayer was not only seeking a profit but actually made substantial profits in selling and leasing its lands and collecting profits and royalties, therefrom. It was therefore doing business and is liable for the tax in question.

ARGUMENT

The taxpayer was engaged in "carrying on or doing business" during the capital stock tax year ended June 30, 1938, within the meaning of Section 601 (a) of the Revenue Act of 1938, and therefore it is subject to excess profits tax liability for the calendar year 1938

As taxpayer properly states (Br. 9), if under the facts herein, it was "carrying on or doing business" for any part of the capital stock tax year from July 1, 1937, to June 30, 1938, then it was liable for the excess profits tax here in dispute on its net income for the calendar year 1938. Sections 601 (a) and 602 (a), Revenue Act of 1938, Appendix, *infra;* Articles 41–44, Treasury Regulations 64 (1938 Edition), Appendix, *infra.* The issue therefore is simply whether or not the taxpayer carried on any business activities during the fiscal year ended June 30, 1938. The taxpayer contends in substance that it did not carry on any such activities during the critical period for the reason that it did none of the things for which it was created but only whatever was reasonably necessary to maintain its corporate existence, conserve its properties and assets and dispose of them in liquidation. (Br. 23–47.) The Board, however, determined (R. 19) that the taxpayer was actually carrying on and doing business in that year and therefore it was liable for the tax in question (R. 17–19). We submit that the findings on which the Board based its conclusion are supported by substantial evidence and that in applying the law to the facts the Board committed no error.

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(a) Under the statute and pertinent regulations and authorities, the taxpayer was carrying on and doing business during the critical period

The statute imposes the excess profits tax for any calendar year if the taxpayer carried on or did business for any part of the capital stock tax year ended the preceding June 30th. Sections 601 (a) and 602 (a), Revenue Act of 1938. The pertinent regulations provide that the tax is imposed upon the privilege of doing business and with respect to the taxpayer's carrying on or doing business, and not upon the business itself as carried on (Article 41, Treasury Regulations 64 (1938 Edition)); that regardless of the nature of the activities, a taxpayer organized for the purpose of profit and carrying out such purpose is doing business, just as it is if not organized for profit so long as it is engaged in activities ordinarily carried on for profit; that it is immaterial whether the activities result in profit or loss, successful or unsuccessful enterprise, or because of unfavorable business conditions no operations are carried on for a particular period, it being unnecessary that any particular amount of business be done or that it be continuous throughout the year; and that only in the most exceptional cases, such as where the corporation is not seeking profit, do the activities amount to its not doing business within the meaning of the act (*id.,* Article 42). As illustrations, the regulations provide that doing business includes such activities as the mere leasing and managing of properties and collecting the rents or royalties, or leasing them to another without divesting oneself of all control and management thereof; the orderly liquidation of property by making sales from time to time and distributing the proceeds therefrom; and any

other activities coming within the ordinary signification of carrying on or doing business. (*Id.*, Article 43 (a), paragraphs 3, 5, 7 and 8, Appendix, *infra.*) Where the corporate powers or its retirement from business limits or reduces the activities to the mere owning and holding of property and the distribution of it avails, the corporation is exempt from the tax, provided, however, that it does not engage in other activities or maintain its organization for the purpose of continued effort in the pursuit of profit or gain; and only where the corporation had no business activities during the entire taxable year because it became dormant or completed or abandoned its business, is it entirely free from the tax. (*Id.*, Article 43 (b), paragraphs 1 and 3, Appendix, *infra.*) These regulations have been sustained as valid. *Magruder* v. *Washington, B. & A. Realty Corp.*, 316 U. S. 69.

Substantially the same regulations as the foregoing have been in effect ever since 1918,[2] covering a long period in which the statute has been reenacted several times.[3] These regulations thus represent a contempo-

[2] Except for the period during which the tax itself was not in existence between 1926 and 1933, these regulations have remained substantially the same since the Revenue Act of 1918, c. 18, 40 Stat. 1057. Article 18, Treasury Regulations 50 (1919 Edition); Article 11, Treasury Regulations 50 (1920 Edition); Article 12, Treasury Regulations 64 (1922 Edition and 1924 Edition); Article 22, Treasury Regulations 64 (1933 Edition); Article 33, Treasury Regulations 64 (1934 Edition); Article 43, Treasury Regulations 64 (1936 Edition); Articles 41–43, Treasury Regulations 64 (1938 Edition).

[3] Revenue Act of 1918, c. 18, 40 Stat. 1057, Section 1000; Revenue Act of 1921, c. 136, 42 Stat. 227, Section 1000; Revenue Act of 1924, c. 234, 43 Stat. 253, Section 700; National Industrial

raneous and long-continued administrative interpretation of the statute and, accordingly, are entitled to great weight. *Brewster v. Gage,* 280 U. S. 327; *Fawcus Machine Co.* v. *United States,* 282 U. S. 375; *McCaughn* v. *Hershey Chocolate Co.,* 283 U. S. 488; *United States* v. *Shreveport Grain & El. Co.,* 287 U. S. 77; *Textile Mills Corp.* v. *Commissioner,* 314 U. S. 326. It is settled that, by clear implication, they have therefore been ratified by Congress and that doubt may not properly be raised as to their validity or the propriety of the departmental practice in applying them over so long a period of time. *White Motor Co.* v. *United States,* 3. F. Supp. 635 (C. Cls.), certiorari denied, 290 U. S. 672; *United States* v. *Safety Car Heating Co.,* 297 U. S. 88, rehearing denied, 297 U. S. 727. In *Magruder* v. *Washington, B. & A. Realty Corp., supra,* the Supreme Court stated, in respect to the same regulations (Article 43 (a) (5), Treasury Regulations 64), the following (pp. 73–74):

> Article 43 (a) (5) is both a contemporary and a long standing administrative interpretation, having been in effect in substantially the same form since 1918, except for the period from 1926 to 1933 when the tax was not imposed. We are of opinion that it is valid, as well as applicable. The crucial words of the statute, "carrying on

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Recovery Act, c. 90, 48 Stat. 195, Section 215; Revenue Act of 1934, c. 277, 48 Stat. 680, Section 701; and the Revenue Acts imposing taxes for the fiscal years ended June 30th, as herein—Revenue Act of 1935, c. 829, 49 Stat. 1014, Section 105; Revenue Act of 1936, c. 690, 49 Stat. 1648, Section 401; and Revenue Act of 1938, c. 289, 52 Stat. 447, Section 601, the latter being identical, as now set forth in Internal Revenue Code, Section 1200.

> or doing business", are not so easy of application to varying facts that they leave no room for administrative interpretation or elucidation. To be sure, in many, if not in most instances, the factual situation will be so extreme as to leave no doubt whether a corporation is doing business or not. But the nuances of facts between the two extremes have produced a nebulous field of confusion which has been recognized by courts striving to fit close cases into one category or the other. Interpretative regulations, such as Article 43 (a) (5), are appropriate aids toward eliminating that confusion and uncertainty. Cf. *Helvering* v. *Wilshire Oil Co.,* 308 U. S. 90, 102; *Textile Mills Securities Corp.* v. *Commissioner,* 314 U. S. 326.

We submit that a consideration of the facts leads inevitably to the conclusion that the taxpayer was carrying on or doing business within the meaning of the statute. The decision is in accord with the regulation interpreting the statute and with the decisions.

Thus, the taxpayer was organized in 1904 to buy, develop and sell land and thereafter acquired more than 16,000 acres of land in connection with which it engaged actively and successfully in the development and sale thereof. (R. 14, 46–47, 51, 56 [4].) The portions of its properties remaining in its hands in the critical fiscal year ended June 30, 1938, constituted a 35-acre tract comprising an orange and lemon grove and 138 acres of unplotted hill lands carried on the taxpayer's books at $52,500 and $13,800, respectively, and reservations of

[4] The record citations, after the Board's findings of fact (R. 14–17), refer to the evidence supporting the findings.

mineral rights in approximately 3,000 acres of lands,[5] previously sold, carried on its books at $1, the 35-acre tract having been abandoned during the fall of 1937 for unpaid state taxes. (R. 15, 58, 60, 62–63, 66, 76, 79, 81–82, 84, 87, 93, 98, 102, 112.) The taxpayer carried on slight business activities during 1930–1935, sold a lot, released oil reservations for $7,500 and entered into negotiations for the leasing of oil rights in 1936. (R. 16, 47, 61, 64–65, 90, 95–96.) During the critical year ended June 30, 1938, however, the taxpayer authorized and placed in escrow a lease (which was not delivered because of the lessee's default), abandoned the above-mentioned grove, sold some fruit, rented pasture lands and had other small activities. Also during that year, it made a loan of $1,500, sold a portion of the hill lands at a profit of $1,890, received $1,180 upon the sale of reserved oil rights, made a 20-year lease of oil rights for royalties which are still being paid to it, realized a total income of $3,270.66, and had expenses and taxes in the aggregate amount of $2,897.34. (R. 16, 71–79, 81–82, 88, 89, 90, 94, 100–101.) After June 30th, but still within the taxable year 1938, the taxpayer continued to pursue its same business activities, having made a lease of oil rights for $20,000 plus royalties from the oil therefrom as long as produced, made a lease for a minimum period of 20 years for $76,130 and the right to royalties therefrom, having paid its agent and attorney

[5] The taxpayer had reserved the mineral rights in selling some of its real estate and authorized its officers to execute oil and gas leases but in 1927 when they ratified the release of the reserved rights in certain land for $2,940, they resolved to make no more such releases "for the present, at least." (R. 15, 89.)

$33,306.88 and $250 for negotiating the lease and preparing the instrument, respectively, and received income from all of its leases and declared dividends in each of the years 1938, 1939 and 1940. (R. 16–17, 55, 84, 86–87, 100–112.) As the Board stated, these later activities showed that the company was ready to do whatever business came its way.

All of the foregoing business operations and activities are shown by the evidence. Thus, the Board's findings as to the taxpayer's activities in the year ended June 30, 1938 (R. 17), were supported by substantial evidence (R. 45–117). Under the regulations and the decided cases, these activities were sufficient to constitute carrying on or doing business.

The taxpayer's purposes of organization and activities, apart from the claimed liquidation aspects of the case dealt with hereafter, unquestionably constituted "carrying on or doing business" within the meaning of the law. Since the first decisions under the 1909 tax on the incomes of corporations "carrying on or doing business", it has been recognized that companies engaged in selling, leasing, and managing real estate are taxable. *Flint* v. *Stone Tracy Co.,* 220 U. S. 107, 169–171[6]; *Von Baumbach* v. *Sargent Land Co.,* 242 U. S. 503; *Page* v. *M. Rich & Bros. Co.,* 99 F. 2d 607 (C. C. A. 5th), certiorari denied, 306 U. S. 662; *Harmar Coal Co.* v. *Heiner,* 34 F. 2d 725, 727 (C. C. A. 3d), certiorari denied, 280 U. S. 610; *United States* v. *Peabody*

[6] A number of the parties to the group of cases passed upon in the opinion in the *Flint* v. *Stone Tracy Co.* case were real estate corporations.

Co., 104 F. 2d 267 (C. C. A. 6th). The taxpayer's activities here had declined as it disposed of its holdings, but it had not ceased the activities for which it was organized. It should be noted that the taxpayer apparently concedes (Br. 24, 29–30) that it was realizing profits from investments.

It is thus clear that since the corporation was organized for profit and was still carrying out the purpose of its organization and had branched into new activities for profit, it was "carrying on or doing business". (See Article 42, Treasury Regulations 64, Appendix, *infra.*) It was also engaged in activities ordinarily carried on for profit, such as the leasing, management and sale of properties. (Articles 42–43.)

It has been frequently declared that the statute "requires no particular amount of business in order to bring a company within its terms". *Von Baumbach* v. *Sargent Land Co., supra,* p. 517; *Page* v. *M. Rich & Bros. Co., supra,* p. 610; *Argonaut Consolidated Mining Co.* v. *Anderson,* 52 F. 2d 55 (C. C. A. 2d), certiorari denied, 284 U. S. 682; *American Investment Securities Co.* v. *United States,* 112 F. 2d 231 (C. C. A. 1st); *Chevrolet Motor Co.* v. *United States,* 64 C. Cls. 211, 222; cf. *Edwards* v. *Chile Copper Co.,* 270 U. S. 452, 455–456 (holding that a taxpayer's entire business purposes, activities and situation must be judged together, and in so doing therein, the taxpayer's merely obtaining money through bond issues and advancing it to its subsidiaries or placing it on call loans constituted doing business and therefore was subject to capital stock tax under the Revenue Acts of 1916 and 1918). In the cases cited the quantity of business carried on by the corporations in-

volved was not substantial, and was fairly comparable to the activities of the taxpayer here. Thus, in the *Von Baumbach* case the corporation had leased its mineral lands, received the rentals, employed another company to inspect the properties for it, and sold and rented certain minor portions of its other real estate. The Court stated (p. 516):

> They were organized for the purposes stated, and their activities included something more than the mere holding of property and the distribution of the receipts thereof. * * *

In the *Chevrolet Motor Co.* case, the court stated (p. 222):

> It is not the volume of business done, although in this case that is a most significant factor, but the real intent and purpose of the activities of the corporation and those engaged in its management and conduct. * * *

The present case is not governed by the regulation (Article 43 (b) (1) and (2))[7] holding the tax inapplicable to corporations engaged in the mere ownership and holding of property and the distribution of the avails, or by decisions holding that a corporation owning or leasing property and doing nothing but distributing the proceeds therefrom to its stockholders is not to be regarded as engaged in business. *Zonne* v. *Minneapolis Syndicate,* 220 U. S. 187; *McCoach* v. *Minehill & S. H. R. Co.,* 228 U. S. 295; *United States* v. *Emery,* 237 U. S. 28.[8] The *McCoach* case, in which a divided court apparently extended this doctrine to such acts necessary

[7] See Appendix, *infra*, pp. 25–26.

[8] The cases cited arose under the 1909 Act.

to the maintenance of the property as the investment and reinvestment of the rentals, seems to have been limited to its facts by many subsequent decisions. Cf. *Von Baumbach* v. *Sargent Land Co., supra; Edwards* v. *Chile Copper Co., supra; United States* v. *Hercules Mining Co.,* 119 F. 2d 288 (C. C. A. 9th), certiorari denied, 314 U. S 658; *United States* v. *Hotchkiss Redwood Co.,* 25 F. 2d 958 (C. C. A. 9th); *Commissioner* v. *Boeing,* 106 F. 2d 305, 309 (C. C. A. 9th); *United States* v. *Trust No. B. I. 35, Etc.,* 107 F. 2d 22 (C. C. A. 9th) (where this Court held that the activities of collecting, caring for and disposing of oil from oil leases conducted through an agent, constituted doing business for profit); *Porter* v. *Commissioner,* 130 F. 2d 276 (C. C. A. 9th); *Argonaut Consolidated Mining Co.* v. *Anderson,* 42 F. 2d 219, 221 (S. D. N. Y.), affirmed 52 F. 2d 55 (C. C. A. 2d), certiorari denied, 284 U. S. 682; *Page* v. *M. Rich & Bros. Co.,* 99 F. 2d 607 (C. C. A. 5th), certiorari denied, 306 U. S. 662; *United States* v. *Peabody Co.,* 104 F. 2d 267 (C. C. A. 6th). In any event the activities of the taxpayer here in selling, renting, and managing real property and the making of oil leases for cash and for present and future royalties, go considerably further than the mere receipt and investment of the proceeds involved in the *McCoach* case.

Subsequent decisions have required very little activity in addition to the holding of property and distribution of the proceeds to bring a corporation within the tax. The test which these cases establish has been sum-

marized by Judge Learned Hand in the *Argonaut* case as follows (p. 56):

> Just what activities bring a corporation within the statutory definition the decisions, as is almost inevitable, do not certainly declare. That there is a degree of quietude which will exempt it, is indeed well settled [*Zonne* v. *Minneapolis Syndicate,* 220 U. S. 187, 31 S. Ct. 361, 55 L. Ed. 428; *McCoach* v. *Minehill, etc., Co.,* 228 U. S. 295, 33 S. Ct. 419, 57 L. Ed. 842; *U. S.* v. *Emery, etc., Co.,* 237 U. S. 28, 35 S. Ct. 499, 59 L. Ed. 825; *Eaton* v. *Phoenix Securities Co.,* 22 F. (2d) 497 (C. C. A. 2); *Rose* v. *Nunnally Co.,* 22 F. (2d) 102 (C. C. A. 3)]; but how far it may be active and still maintain its exemption, is in the nature of things impossible of statement in general terms. In most of those cases in which the corporation has succeeded its activities have been confined to holding the title of property, whose usufruct it receives and distributes in dividends. When this is the whole scope of its dealings, it does no business within the meaning of the statute.
>
> However, it takes little to bring it from behind this shield. Thus, selling and leasing land, and exploring for ore, were enough in *von Baumbach* v. *Sargent Land Co.,* 242 U. S. 503, 37 S. Ct. 201, 61 L. Ed. 460; and borrowing money to assist the subsidiary in *Edwards* v. *Chile Copper Co.,* 270 U. S. 452, 46 S. Ct. 345, 70 L. Ed. 678. On the other side the investment of its funds in current securities from which income is derived was not enough in *McCoach* v. *Minehill, etc., Co.,* 228 U. S. 295, 33 S Ct. 419, 57 L. Ed. 842.

The test to be applied is, whether a corporation is (*id.*, at 57) "outside the class of those inert companies, which can assert that they are mere dry holders of property, and conduits to carry over its profit to the persons eventually entitled." See also *American Investment Securities Co.* v. *United States,* 112 F. 2d, at 233.

The activities and expenditures of the taxpayer as outlined above clearly show that it does not come within the class of "inert" or "dry holders of property" which are exempt from the law. Rather, as stated in *Edgar Estates Corp.* v. *United States,* 65 C. Cls. 415, 423—

> If the corporation was pursuing the object for which it was organized and doing all the essential things to accomplish that object, it can not claim a classification of an inactive corporation * * *.

Finally, the taxpayer's erroneous contention that it was not doing business during the critical period herein was aptly answered by this Court in a somewhat comparable situation in *United States* v. *Trust No. B. I. 35, Etc., supra,* as follows (p. 26):

> A further false premise is that the owner of oil land, some leased and some free to lease, with oil sands developed at a certain depth and (in Kern County) the contemplated possibility of still deeper deposits, is not engaging in a productive business for profit when its lessee extracts the oil, but is merely liquidating its capital investment. To state the proposition is to refute it. * * *

(b) Even if the taxpayer merely intended to maintain and preserve its properties with the intention of liquidating them, it was nevertheless carrying on and doing business for profit and therefore taxable

The taxpayer further contends, substantially, that its activities during the year ended June 30, 1938, comprised merely isolated transactions, not for the purposes for which it was organized, but rather reasonably related to the maintenance and preservation of its properties and the orderly disposal and liquidation thereof as rapidly as conditions reasonably warranted, and therefore it is not subject to the tax in question. (Br. 47–72.)

Even if the taxpayer intended to liquidate over a long period of time and carried on its business activities with that end in view, the fact nevertheless remains that corporate activities consisting of liquidation of assets do not mean that it is not engaged in business. In a sense, every mining or other wasting-asset corporation is engaged in the liquidation of its assets.[9] The real question, we submit, is not whether a corporation *intends* to continue doing business after the property presently owned is disposed of, but whether it *is* doing business at the time it is disposing of the property. The nature of the activities during the taxable period, not the intention as to what the corporation will or will not do in the future, must be controlling. We have al-

[9] The taxability of a wasting-asset corporation is clear. Cf. *Harmar Coal Co.* v. *Heiner*, 34 F. 2d 725 (C. C. A. 3d), certiorari denied, 280 U. S. 610; *United States* v. *Hercules Mining Co.*, 119 F. 2d 288 (C. C. A. 9th), certiorari denied, 314 U. S. 658; *Lyon Lumber Co.* v. *Harrison*, 113 F. 2d 443 (C. C. A. 7th).

ready shown heretofore that, under the authorities and the pertinent regulations, the taxpayer was actually doing business during the critical period.

Moreover, if in addition to the business activities carried on by the taxpayer, it was also engaged in liquidation at the same time, then the regulation specifically provides that any activities it engaged in towards the orderly liquidation of its property by negotiating sales from time to time as opportunity and judgment dictated and the distribution of the proceeds as the liquidation was effected, constituted "doing business" within the meaning of the statute. Art. 43 (a)(5), Treasury Regulations 64 (1938 Ed.), *infra.* It is settled that this regulation is valid and must be given effect. *Magruder* v. *Washington, B. & A. Realty Corp., supra.*

The Board correctly held that the taxpayer's argument is concluded by that case, regardless of whether or not earlier cases held to the contrary. (R. 17–18.) There, the corporation was formed for the purpose of liquidating the properties in question, formerly belonging to a defunct corporation. The Court, holding valid and applying the above regulation, concluded that the taxpayer was actively engaged in fulfilling the purposes of its creation—liquidation of its holdings for the best obtainable price—and therefore it was carrying on and doing business within the meaning of Section 105 (a) of the 1935 Act (identical with Section 601 (a) of the 1938 Act herein, except for years and amounts). Consequently, the Court upheld the imposition of the capital stock tax for the years 1936–1939 and denied the refund claimed by the taxpayer.

The taxpayer contends that the Board misinterpreted and misapplied the decision in that case to the facts herein on the ground that the regulations (Art. 43 (b) (2), Treasury Regulations 64 (1938 Ed.)) exempt from tax a corporation which is merely holding property, distributing its avails, and maintaining its corporate status, whether the corporation was organized for such purposes or has reduced its activities to the mere owning and holding of the property and the distribution of the avails thereof. (Br. 40–45). We have already shown, however, that the taxpayer was formed for the purpose of, and was actually, carrying on and doing business for profit and that instead of merely holding property, the business activities and profits were increasing during the tayable year 1938. *Continental Baking Corp.* v. *Higgins,* 130 F. 2d 164 (C. C. A. 2d), the principal case relied upon by the taxpayer (Br. 44–45), is distinguishable for somewhat the same reasons that the Court found it distinguishable from *Magruder* v. *Washington, B. & A. Realty Corp., supra.* There, the activities of the taxpayer—sale and exchange of its own and its subsidary's stock in order to liquidate and eliminate an intermediate holding company as a step in its plan of consolidation—were, unlike the taxpayer's herein, "only those of a quiescent holding company such as fall within the exceptions set forth in Treasury Regulations 64, Article 43 (b), (2), and not within Article 43 (a), (5), as did those dealt with in *Magruder, Collector* v. *Washington, B. & A. Realty Corp., supra.*" (P. 167.)

In view of the foregoing, we submit that under the facts herein the taxpayer was clearly engaged in, carry-

ing on and doing business within the meaning of Section 601 (a) of the 1938 Act, rather than merely performing incidental and isolated transactions necessary for the preservation and liquidation of its properties. It is therefore liable for the tax imposed under Section 602 (a) of that Act for the taxable year 1938, as the Board held.

CONCLUSION

The decision of the Board of Tax Appeals is correct and in accord with law and the authorities. It should therefore be affirmed.

Respectfully submitted,

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DECEMBER, 1942.

argued by Mr. Rockwell

APPENDIX

Revenue Act of 1938, c. 289, 52 Stat. 447:

SEC. 601. CAPITAL STOCK TAX.

(a) For each year ending June 30, beginning with the year ending June 30, 1938, there is hereby imposed upon every domestic corporation with respect to carrying on or doing business for any part of such year an excise tax of $1 for each $1,000 of the adjusted declared value of its capital stock.

* * * * *

SEC. 602. EXCESS-PROFITS TAX.

(a) If any corporation is taxable under section 601 with respect to any year ending June 30, there is hereby imposed upon its net income for the income-tax taxable year ending after the close of such year, an excess-profits tax equal to the sum of the following:

"6 per centum of such portion of its net income for such income-tax taxable year as is in excess of 10 per centum and not in excess of 15 per centum of the adjusted declared value;

"12 per centum of such portion of its net income for such income-tax taxable year as is in excess of 15 per centum of the adjusted declared value."

* * * * *

Treasury Regulations 64 (1938 Edition), relating to the Capital Stock Tax:

ARTICLE 1. *Effective date of the tax.*—The capital stock tax imposed by section 601 of the Revenue Act of 1938 is in effect on and after July 1, 1937, and applies with respect to each

year ending June 30, beginning with the year ending June 30, 1938.

ART. 41. *Nature and rate of tax.*—The tax is an excise tax imposed with respect to carrying on or doing business during a taxable year ending June 30, or any fractional part thereof. It is an excise tax upon the exercise of the privilege of doing business and not upon the business itself and is imposed upon each corporation with respect to carrying on or doing business and not upon each business carried on. If more than one corporation is engaged in carrying on a single business, each must file a return and pay the tax. The tax is imposed at the rate of $1 for each full $1,000 of the adjusted declared value of the capital stock. The tax may not be apportioned under any circumstances. If a corporation is engaged in business for any portion of a taxable year, liability for the tax is incurred for the entire taxable year.

ART. 42. *Doing business.*—The term "business" is very comprehensive and embraces whatever occupies the time, attention, or labor of men for profit. Accordingly, regardless of the nature of its activities, any corporation organized for profit and carrying out the purpose of its organization is doing business within the meaning of the Act. Similarly, even if not organized for profit, any corporation which engages in activities ordinarily carried on for profit is doing business. It is immaterial whether the activities result in a profit or a loss, or whether the corporation has been successful in its enterprise, or that because of unfavorable business conditions, no operations are carried on for a particular period. No particular amount of business need be done, nor is it necessary that the business be continuous throughout the taxable year.

The case is exceptional in which the activities of a corporation organized for profit do not amount to doing business within the meaning of the Act. Such a case is generally limited to one

in which the corporation is not pursuing the ends for which organized, i. e., profit.

ART. 43. *Illustrations.*—(a) *General.*—In general "doing business" includes any activities of a corporation whether it engages in—

* * * * *

"(3) leasing or managing properties, collecting rents or royalties;

* * * * *

"(5) the orderly liquidation of property by negotiating sales from time to time as opportunity and judgment dictate and distribution of the proceeds as liquidation is effected—for example, the liquidation of an estate, or of properties taken over from another corporation, or of the shareholders' fractional interests in particular property;

* * * * *

"(7) leasing all its properties to another without divesting itself of all control and management of the properties under such terms that it keeps the properties in repair, or engages in other activities necessary to enable the lessee to utilize the leased properties, regardless of whether such activities are performed on behalf and under the order of the lessee or whether such acts are of major importance; or

"(8) any other activities coming within the ordinary and natural signification of the term 'carrying on or doing business'."

(b) *Exceptions.*—Ordinarily the exceptions to "doing business" are restricted to limited activities of a corporation. For example—

(1) A corporation is not subject to the tax if its corporate powers are limited to the mere owning and holding of property and the distribution of its avails, or, although incorporated for the purpose of doing business, if it has retired from the business for which it was organized and has reduced its activities to the mere ownership and holding of property, the distribution of its avails,

and doing only such acts as are necessary to the maintenance of its corporate existence and the private management of its purely internal affairs. However, a corporation which has retired from its principal business is subject to the tax if, nevertheless, it engages in other business activities or maintains its organization for the purpose of continued effort in the pursuit of profit or gain.

(2) A corporation may complete its organization and sell its capital stock for cash without incurring liability. However, the exchange of its capital stock for property other than cash or the use of the proceeds from the sale of its capital stock for the purchase of property are corporate business acts and constitute doing business. Entering into contracts for the purchase of property or the construction of a plant are also corporate acts and constitute doing business. In other words, it is not necessary that a corporation be actually engaged in the manufacture of its intended product or that it be actually creating profit or gain to incur liability, since making contracts, buying materials or machinery, and employing and discharging individuals are necessary business acts leading to the ultimate attainment of the objects and purposes for which the corporation was created and has its existence.

(3) A corporation will not be regarded as "doing business" if it had no activities during entire taxable year, because it has—

"(a) become dormant; or

"(b) completed its business, as, for example, where a real estate subdivision has been developed, sold and reduced to cash; or

"(c) abandoned its business, as, for example, where prospective oil properties are proven worthless"

ART. 44. *Declared value.*—In its return for each declaration year, a corporation must declare a definite and unqualified value for its

capital stock. The declaration of value must be made in terms of United States dollars and be specific, as, for example, $10,000, or "Zero," in the event it is desired to indicate no value. Inasmuch as the declared value can in no case be less than zero, a declaration of a deficit or minus figure shall be considered a declaration of "Zero."

* * * * *

For the declared value of corporate capital stock referred to in Article 44, *supra,* and the declared value excess-profits taxes regulation relating to the excess-profits taxes imposed by Section 602 of the Revenue Act of 1938, see T. D. 4829, 1938–2 Cum. Bull. 98.

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